ORIGINAL

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992 Rate Regulation	))))))))	MM Docket No. 93-215

RECEIVED

JUL 11 1994

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

COMMENTS OF RAINBOW PROGRAMMING HOLDINGS, INC.

Rainbow Programming Holdings, Inc., ("Rainbow"), by its attorneys, submits these comments in response to the Report and Order and Further Notice of Proposed Rulemaking in the above-captioned proceeding.[1/]

Rainbow, a wholly-owned subsidiary of Cablevision Systems Corporation ("Cablevision"), is the managing general partner of several partnerships[2/] that provide national and regional programming available to more than 120,000,000 subscribers. Rainbow's programming services include American Movie Classics, Bravo Network, News 12 Long Island (a regional news service

---

[1/] In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 93-215 (rel. March 30, 1994)("Cost of Service Order" or "Further Notice").

[2/] Subsidiaries of the National Broadcasting Company ("NBC") are general partners in most of the partnerships; subsidiaries of Liberty Media Corporation ("Liberty"), which holds interests in several other programming services, are general partners in several of the regional sports services and Prime SportsChannel Networks. Each of the programming services is organized as a separate partnership with its own general manager and sales, marketing, programming, and production staffs. Rainbow provides legal, accounting, human resources, and other support services for all of the partnerships.

No. of Copies rec'd 0+5
List ABCDE

serving Long Island), MuchMusic, eight regional SportsChannel services, the national backdrop sports services of Prime SportsChannel Networks, and Prism, a premium sports and movie service serving the Philadelphia market.[3/]

INTRODUCTION

In the Further Notice, the Commission has proposed that cable operators affiliated with a programmer selling more than 25 percent of its "output" to affiliates would be barred from using prevailing company pricing to establish subscriber rates.[4/] Rather, affiliated cable operators would be required to value the programming at the lesser of its cost to the provider or its estimated fair market value in determining the amount of programming costs that could be passed through to subscribers.[5/]

The proposed limit on prevailing company pricing -- drawn almost verbatim from a pending proposal to govern affiliate transactions by telcos -- is wholly unnecessary to protect cable subscribers and will seriously disrupt the programming marketplace. In contrast to the telephone industry, there is no record of collusive transfer-pricing schemes between vertically integrated affiliates in the cable industry that warrants the adoption of this rule. To the contrary, adoption of the proposal would disserve the public interest by jeopardizing continued

---

3/ Services soon to be launched include Romance Classics, the Independent Film Channel, and the Singles Network.

4/ Further Notice at ¶ 310.

5/ Id.

revenues for programming such as Rainbow's regional sports services and its award-winning News 12 on Long Island.

Only last year, the Commission reconsidered and abandoned a rule that limited an operator's ability to pass through increases in the costs of programming obtained from affiliates because it feared that the rule would dampen the continued growth of programming. The current proposal would unravel vertical relationships between operators and programmers, which the Commission has already sanctioned,[6] and reestablish the same disincentives for program creation and expansion that the Commission sought to eliminate then. To the extent that operators and affiliated programmers actually collude to set artificial prices for programming, they would be subject to antitrust laws and the anti-evasion provisions of the Cable Act.[7] The proposed rule should be rejected.

ARGUMENT

Because of the definition of affiliate that it intends to utilize,[8] the sweep of the Commission's proposed limit on the use of prevailing company pricing will affect a substantial number of vertically-integrated cable operators. For example, certain of Rainbow's sports programming services likely will be

---

[6] 47 C.F.R. § 76.504 (permitting operators to own interests in up to 40% of the programming channels carried on their systems).

[7] 47 U.S.C. § 543(h).

[8] Further Notice at n. 577; Cost of Service Order at ¶ 269; 47 C.F.R. § 76.1000(b).

deemed to affiliate with both Cablevision and TCI.[9/] Accordingly, despite the fact that sales to non-affiliates constitute well over half of the output of Rainbow's sports programming services, its affiliated cable operators will be unable to value the service on their books at the prevailing company price. Likewise, News 12, the nation's first regional news service, is provided almost entirely to systems owned and operated by Cablevision, simply because the geographic scope of its news coverage focuses chiefly on Long Island, where Cablevision is the principal operator. News 12 has never experienced positive cash flow in any fiscal year, yet it could face significant additional revenue shortfalls if Cablevision reduced its payments for the service to match the valuation decrease on its books necessitated by the rule.

Vertical integration in the cable industry arose because of subscriber demands for a broader range of programming. Unlike the telephone industry,[10/] vertically-integrated programming affiliates were not created solely to service the parent company with generic inputs. Rather, vertically integrated cable programmers provide value to a cable operator, affiliated or

---

[9/] Ironically, in light of the stated rationale for the pending proposal, many of Rainbow's services were initiated long before Liberty Media, an affiliate of TCI, invested in them. Moreover, Prism and SportsChannel New England were not created by Rainbow, but were purchased by the company. Yet under the Commission's proposal, these services will be deemed to have been created primarily to serve an operator <u>that was not even affiliated</u> with the services at their inception.

[10/] See infra at p. 7.

unaffiliated, by contributing the diverse programming mix necessary to attract and expand the operator's subscriber base.

By limiting an affiliated operator's programming costs to the lesser of the programmer's net book cost or fair market value of the programming, the Commission would deprive programmers of a significant source of the revenues they need to continue to produce and develop programming. Assuming that Rainbow's cable partners will be unwilling to incur substantial losses by continuing to pay Rainbow the prevailing company price for carrying cable channels which they own, the affiliated operators will either be forced to drop such programming services from regulated tiers or to engage in distress sales of such services in order to ensure that they can realize adequate cash flows. Each of these outcomes severely damages the interests of both subscribers and programmers.

The Commission's proposed limit on an operator's ability to establish programming costs on the basis of prevailing company pricing will, in effect, reestablish the same disincentives for programming creation and expansion that the Commission sought to eliminate in the First Order on Reconsideration.[11/] There, the Commission abandoned its proposal to limit an operator's ability to fully recover increases in affiliated programming expenses because of fears that it would dampen "the continued growth of

[11/] See In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, First Order on Reconsideration, MM Docket No. 92-266 (rel. August 27, 1993) ("First Order on Reconsideration") at ¶ 114.

programming."[12/] Instead, the Commission determined that allowing operators to pass-through increases in programming expenses based upon prevailing company prices would better promote a strong and diverse programming market.[13/] The Commission's arbitrary determination that a programmer must make 75 percent of its sales to unaffiliated cable operators in order for affiliates to utilize the prevailing company price substantially and unnecessarily restrict many affiliated programmers from using the very tool that the Commission determined would help strengthen the programming marketplace.

There is no historical or factual basis for the Commission's apparent conclusion that operators and their affiliated programmers will engage in collusive transfer-pricing schemes to artificially raise cable rates.[14/] In the absence of such a factual record, adoption of the proposed limitation would be arbitrary and capricious.[15/] To the extent that operators and programmers collude to set wholesale programming prices at supra-

---

[12/] Id.

[13/] See id.

[14/] See Further Notice at ¶ 310-311. As the Commission suggests, the "prevailing company price" itself is an artificial constraint designed to prevent transfer-pricing schemes between affiliates. See Cost of Service Order at ¶ 267. In the absence of a record of transfer pricing between operators and their programming affiliates, however, there is no basis for imposing any valuation method on cable affiliate transactions.

[15/] Cf. Turner Broadcasting Co. v. FCC, 62 U.S.L.W. 4647, 4659 (June 27, 1994) (remanding must-carry provisions because of "paucity of evidence" supporting their necessity); see Home Box Office Inc. v. FCC, 567 F.2d 9, 37 (D.C. Cir. 1977) (invalidating anti-siphoning rules because of lack of evidentiary basis).

competitive levels to produce higher retail cable rates, they risk violating both the Commission's anti-evasion rules and the antitrust laws.

The paucity of the record in the instant proceeding contrasts starkly with the substantial record in the telephone industry detailing transfer pricing schemes between the Bell Operating Companies and their affiliates.[16] In the telco context, the proposed limit on the use of prevailing company pricing arose in response to well-publicized cases in which BOC subsidiaries were created for the sole purpose of supplying the regulated parent company with generic inputs such as office supplies and other materials easily available from alternative sources.[17] Such circumstances are wholly distinct from -- and irrelevant to -- the relationship between operators and their programming affiliates in the cable industry.

---

[16] See e.g. United States v. AT&T, 552 F.Supp. 131, 161-63 (D.D.C. 1982), aff'd sub nom., Maryland v. United States, 460 U.S. 1001 (1983); Dr. Mark N. Cooper, Divestiture Plus Eight: The Record of Bell Company Abuses Since The Break-up of AT&T, Consumer Federation of America, December 1991.

[17] See e.g., In the Matter of New York Telephone Co., Apparent Violations of the Commission's Rules and Policies Governing Transactions With Affiliates, 5 FCC Rcd. 5892 (1990)(NYNEX agreed to pay a $1.42 million fine for alleged improper use of ratepayer money to cross-subsidize a subsidiary), recon. denied, 6 FCC Rcd. 3303 (1991), aff'd 71 R.R. 2d 1260 (D.C. Cir. 1993).

CONCLUSION

For the foregoing reasons, the Commission should abandon its proposal to limit a cable operator's ability to utilize the prevailing company price charged by affiliated programmers.

Respectfully submitted,

RAINBOW PROGRAMMING HOLDINGS, INC.

Howard J. Symons / CJH

Howard J. Symons
Christopher J. Harvie
Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C.
701 Pennsylvania Ave., N.W.
Suite 900
Washington, D.C. 20004
202/434-7300

Its Attorneys

Of Counsel:

Hank J. Ratner
Executive Vice President - Legal and Business Affairs
Rainbow Programming Holdings, Inc.
150 Crossways Park West
Woodbury, NY 11797

July 1, 1994

D29283.2